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PACKERS AND
STOCKYARDS
PROGRAMS

Investigations of
Competitive Practices
Need Improvements

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Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to testify on the work we have completed on the U.S. Department of Agriculture's (USDA) efforts to investigate concerns about competition in the marketing of cattle and hogs. Our testimony today is based on our September 21, 2000, report entitled *Packers and Stockyards Programs: Actions Needed to Improve Investigations of Competitive Practices* (GAO-RCED-00-242), which you requested. As you know, within USDA, the Grain Inspection, Packers and Stockyards Administration (GIPSA) is responsible for investigating concerns about unfair and anticompetitive practices in the \$43 billion cattle and hog market.

Our testimony today focuses on the three areas covered in our report: (1) the number and status of investigations conducted by GIPSA in response to complaints and concerns about anticompetitive activity involving the marketing of cattle and hogs, (2) factors that affect GIPSA's ability to investigate concerns about anticompetitive practices, and (3) GIPSA's authority under the Packers and Stockyards Act to address concerns about anticompetitive and unfair practices. In summary, we found the following:

- From October 1, 1997, through December 31, 1999, GIPSA investigated 74 allegations or concerns about anticompetitive activity involving cattle or hogs. At the end of March 2000, 57 of these investigations had been completed, and the remaining 17 were ongoing. GIPSA identified a total of five alleged violations of the Packers and Stockyards Act. These violations involved acts by one or a few companies in such areas as deceptive pricing.
- GIPSA has strengthened its ability to address competition concerns since a highly critical report was issued by USDA's Inspector General in 1997. However, two principal factors continue to detract from GIPSA's ability to investigate concerns about anticompetitive practices in these markets. First, the agency's investigations are planned and conducted primarily by economists without the formal involvement of attorneys from USDA's Office of General Counsel (OGC). As a result, a legal perspective that focuses on assessing potential violations is generally absent when investigations are initiated and conducted. Second, GIPSA's investigative processes and practices are designed for the traditional trade practice and financial issues that

the agency has emphasized for years and are not suited for the more complex competition-related concerns that it is also now addressing.

- USDA has authority under the Packers and Stockyards Act, which has been delegated to GIPSA, to initiate actions to halt unfair and anticompetitive practices by meatpacking companies and by other parties involved in livestock marketing. Specifically, the agency can take action to stop companies from engaging in or using any unfair, unjustly discriminatory, or deceptive practice or device, or making or giving any undue or unreasonable preference or advantage to another party. In addition, the agency can take action to halt unlawful anticompetitive practices that are antitrust-type actions, such as a packer's activities that manipulate or control prices or restrain trade.

In our report, we recommended several actions to improve GIPSA's investigations. Specifically, we recommended that USDA integrate the attorneys from OGC into GIPSA's investigative teams. The teamwork approach used at the Department of Justice (DOJ) and the Federal Trade Commission (FTC) to perform comparable investigations of anticompetitive practices would benefit GIPSA's investigations. We also recommended that GIPSA adopt more systematic approaches to its investigative work, including approaches on how cases are selected and investigations conducted.

Mr. Chairman, we are encouraged by USDA's positive response to our draft report. The Department concurred with our recommendations and spelled out specific steps that it is considering in responding to the problems that we identified.

Background

The Packers and Stockyards Act was passed in 1921 in response to concerns that, among other things, the marketing of livestock presented special problems that could not be adequately addressed by the federal antitrust laws existing at that time. The act's provisions were based, in part, on prior antitrust statutes, including the Sherman Act and the Federal Trade Commission Act. GIPSA is responsible for implementing the Packers and Stockyards Act. USDA's OGC also has a role in enforcing the act and, among other

activities, represents the Department in administrative and court proceedings addressing alleged violations of the act.

In general, DOJ and FTC are responsible for enforcing federal antitrust laws that protect the marketplace from practices that adversely affect competition. DOJ is responsible for enforcing the Sherman Act, and FTC has responsibility for the Federal Trade Commission Act.¹ If GIPSA identifies an activity that appears to be criminal or a violation of antitrust law, GIPSA officials may consult with DOJ on whether the case should be forwarded to DOJ for action. DOJ and FTC also share responsibility for reviewing proposed mergers under the Clayton Act.²

In 1996, GIPSA reported that dynamic changes had taken place in the cattle and hog industries in recent years, including increasing concentration and vertical integration—where packers own the animals. GIPSA stated that these changes had reduced the role of public markets, where terms of a trade are visible to all. GIPSA also reported that past studies were inconclusive about whether the industry remained competitive. Also, in 1996, an advisory committee to the Secretary of Agriculture reviewed the concerns of producers and others about the changes in livestock markets and recommended, among other things, a review of GIPSA's efforts to enforce the Packers and Stockyards Act. The Secretary of Agriculture then asked USDA's Office of Inspector General (OIG) to review GIPSA's program.

In 1997, USDA's OIG reported that GIPSA had a credible record of investigating claims of fraud and unfair business dealings, such as false weighing and failing to pay for livestock. However, the report stated that GIPSA (1) did not have the capability to perform effective anticompetitive practice investigations and (2) faced formidable obstacles to become effective in performing such investigations because it had not been organized, operated, or staffed for this purpose. The Inspector General stated that GIPSA should employ an approach similar to that used by DOJ and FTC, and integrate attorneys and economists from the beginning of the investigative process.

¹FTC has a specific responsibility under the Packers and Stockyards Act to address anticompetitive and unfair practices in retail sales of meat and meat products.

²The Packers and Stockyards Act does not provide USDA with premerger review authority. However, GIPSA may initiate administrative actions to halt unfair and anticompetitive practices of a company formed by a merger.

In response, GIPSA completed a major restructuring of its headquarters and field offices in 1999 and hired staff to strengthen its investigations of alleged anticompetitive practices. GIPSA now has regional offices in Denver, Colorado, for its work on the cattle industry; in Des Moines, Iowa, for handling work on the hog industry; and in Atlanta, Georgia, for its work on the poultry industry. During the reorganization, GIPSA experienced substantial employee changes: Over 40 staff relocated, and 44 staff left the agency. Also, the agency hired 67 new employees from April 1998 through July 2000, including economists and legal specialists to assist with its investigations of competitive practices.

Recent GIPSA Investigations Has Found Little Anticompetitive Activity

Our review disclosed that GIPSA has found few instances of anticompetitive activity in recent years. Specifically, GIPSA conducted 74 investigations involving concerns about potential anticompetitive activity in the cattle and hog markets from October 1, 1997, through December 31, 1999, and identified alleged anticompetitive actions in only 5 cases.³ (See table 1.) The alleged violations involved acts by specific meatpacking companies, such as deceptive pricing, rather than industrywide practices. Thirty-six of these investigations were in direct response to specific complaints about anticompetitive actions; the other 38 cases were initiated by GIPSA.

³We did not evaluate the effectiveness of GIPSA's efforts and findings in these cases.

Table 1: Results of GIPSA's Investigations of Allegations of Anticompetitive Actions From the Start of Fiscal Year 1998 Through the First Quarter of Fiscal 2000

Alleged violator and type of animal	Number of investigations	Status of investigation		Did GIPSA find anticompetitive action?	
		Open	Closed	Yes	No
Meatpacking company					
Cattle	39	11	28	3	27
Hogs	12	6	6	2	7
Subtotal ^a	51	17	34	5	34
Other ^b					
Cattle	21	0	21	0	21
Hogs	2	0	2	0	2
Subtotal	23	0	23	0	23
Total					
Cattle	60	11	49	3	48
Hogs	14	6	8	2	9
Total	74	17	57	5	57

Note: The information on the status of investigations and whether GIPSA found anticompetitive actions is as of the end of March 2000.

^aThe total number of cases where GIPSA did or did not find anticompetitive actions exceeds the total number of closed cases because three cases in which anticompetitive actions were reported remained open for resolution at the time of our review and two cases in which anticompetitive actions were not found remained open for an informational review at the agency's headquarters.

^bIncludes livestock markets, dealers, and others who buy or sell livestock on commission.

Source: GAO's analysis of information obtained from GIPSA's complaint/investigation automated system, the agency's files and records, and the agency's officials.

During this period, GIPSA also conducted various other examinations that were designed primarily to develop information about the cattle and hog markets, including how prices for animals are determined. Specifically, a major examination of cattle buying in Texas was completed in 1999; another involving the procurement of hogs in four states in the Western Cornbelt was completed in 1998.⁴ Neither found violations of the Packers and Stockyards Act.

Two Principal Factors Detract From GIPSA's Capability to Fully Investigate Concerns About Competition

We identified two principal factors that detract from GIPSA's capability to investigate anticompetitive practices. The first factor concerns the composition of GIPSA's investigative teams. We found that attorneys from USDA's OGC are not directly involved

in GIPSA's investigative work and the economists that GIPSA has hired since 1998 are inexperienced in investigative work. The second factor we identified is that GIPSA does not have investigative processes and practices appropriate for conducting complex anticompetitive practice investigations.

Attorneys' Participation in Investigations

GIPSA relies on USDA's OGC attorneys for legal advice, and OGC reviews the results of GIPSA's investigations to determine if violations of law might have occurred. However, OGC attorneys usually do not participate at the start or throughout the agency's investigations. OGC attorneys are not assigned until GIPSA has performed an investigation and forwarded a developed case file to them for review and action. The agency's investigations are planned and conducted primarily by economists, most of whom have limited investigative experience.

In contrast, DOJ and FTC have teams of attorneys and economists to perform investigations of anticompetitive practices. Attorneys are assigned to lead and conduct the investigations from the outset so that a legal perspective is focused on assessing potential violations of law, and economists are routinely assigned as an integral part of the investigation teams. These agencies use this approach so that a legal perspective is brought to bear on the interpretation of law, development of evidence, and preparation of cases for presentation in administrative and judicial proceedings.

We also found that OGC officials have provided GIPSA with informal assistance in the investigations, but this assistance has been limited and has declined along with the number of OGC attorneys assigned to assist GIPSA. Since 1998, the number of OGC attorneys assigned to GIPSA's cases has decreased from eight to five because of budget constraints, according to USDA's General Counsel. Also, these attorneys are not all assigned full-time to GIPSA's financial, trade practice, and competition cases; some are assigned to responsibilities in other USDA areas as well. OGC officials told us that at least six full-time attorneys are needed for GIPSA's casework and the agency's reorganization plan called for up to eight attorneys.

⁴GIPSA published the results of these examinations in papers entitled *Investigation of Fed Cattle Procurement in the Texas Panhandle* (Dec. 28, 1999) and *Western Cornbelt Hog Procurement Investigation* (Oct. 8, 1998).

Furthermore, GIPSA has had difficulty recruiting economists with specialties that are particularly useful in anticompetitive practice investigations. The grade levels that GIPSA has offered for these positions (up to GS-11) are not competitive with the grade levels offered by other agencies such as DOJ and FTC (up to GS-15). Also, the legal specialist position that GIPSA developed appears to be more limited than anticipated. USDA's General Counsel informed GIPSA that (1) its legal specialists can assist on investigations but that they are not lawyers for GIPSA and cannot give legal opinions even if they have law degrees and (2) only OGC's lawyers are authorized to provide legal services in support of all USDA activities. In addition, the legal specialists in GIPSA's field offices are not supervised by attorneys.

In our report, we concluded that GIPSA's program has additional steps to take to become more effective and efficient in performing investigations. One step forward would be to integrate OGC's attorneys into GIPSA's investigative teams. A teamwork approach has been used at DOJ and FTC and would also be beneficial in GIPSA's investigations. In addition, the role of GIPSA's legal specialists could be strengthened if they have the leadership and supervision of OGC's attorneys, and GIPSA may also be able to improve its recruitment of economic specialists. Therefore, we recommended that the Secretary of Agriculture develop a teamwork approach for investigations with GIPSA's economists and OGC's attorneys working together to identify violations of the law. We also recommended that the Secretary (1) determine the number of attorneys that are needed for USDA's OGC to participate in GIPSA's investigations and, as needed, assign attorneys to lead or participate in the investigations, (2) ensure that legal specialists are used effectively by providing them with leadership and supervision by USDA's OGC attorneys, and (3) ensure that GIPSA has the economic talents it requires by considering whether to modify the GS grade structure for GIPSA's economists.

Processes and Practices for Anticompetitive Practice Investigations

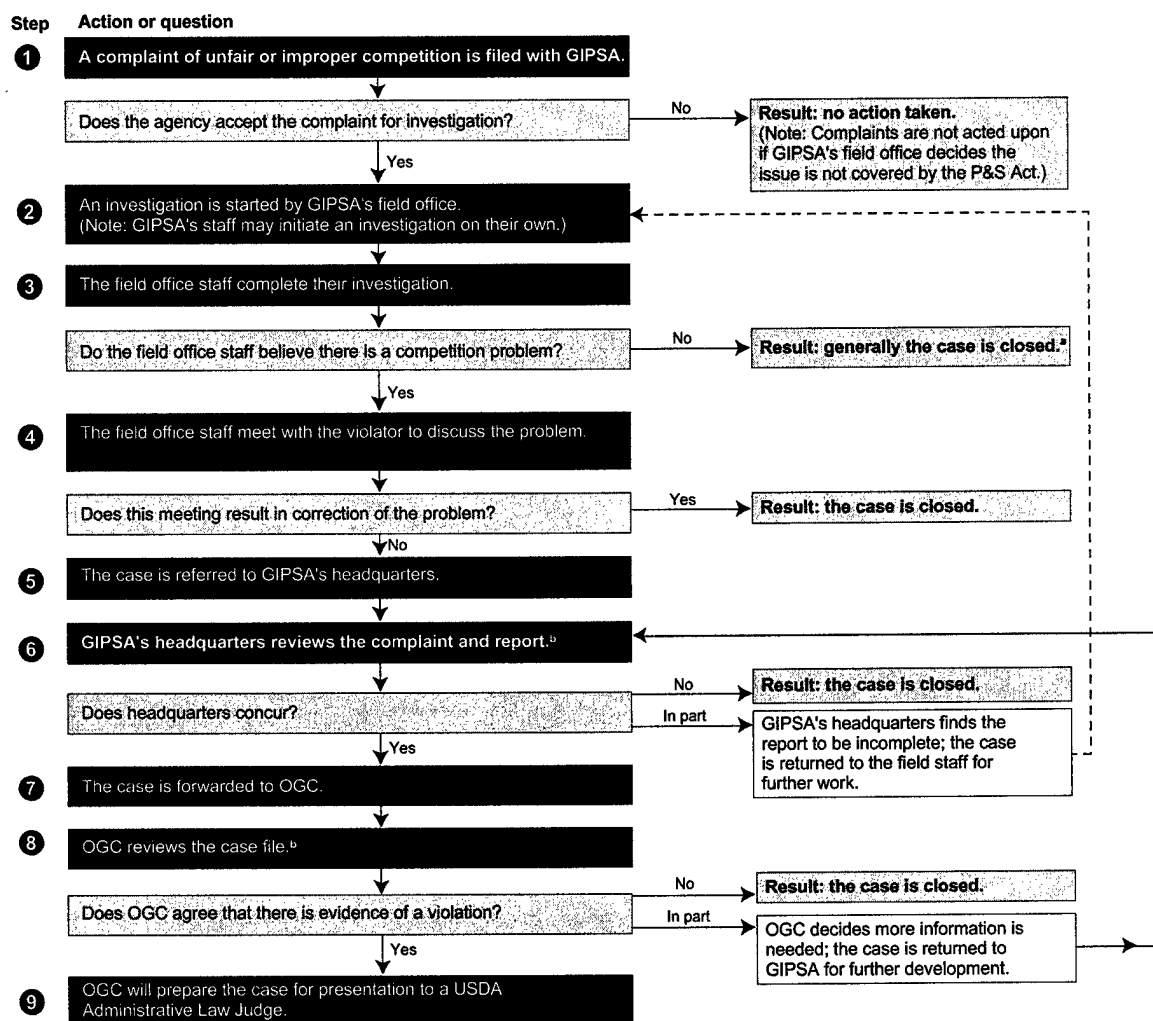
The second factor affecting GIPSA's capabilities is that its investigative processes and practices were not designed for addressing complex anticompetitive practice concerns—they were designed for the trade practice and financial issues that the agency has

emphasized for years. In comparison, DOJ and FTC have processes and practices specifically designed for guiding investigations of competition-related issues.

DOJ and FTC emphasize establishing the theory of each case and the elements that will prove a case. At each stage of an investigation, including selecting the case, planning, and conducting the investigation, there are reviews by senior officials—who are attorneys and economists—that focus on developing sound cases. For example, DOJ and FTC require their attorneys, assisted by economists, to establish a theory explaining how a company's (or companies') behavior may be a violation of the law. The case theory and evidence are reviewed by senior officials after a preliminary inquiry, prior to approving an investigation, and then periodically as the factual underpinnings of the case come into focus as the investigation proceeds. The plan is to consider all the evidence that may be needed to determine if there is a violation. The theory of the case and an outline of proof are revised through the course of an investigation.

In contrast to DOJ and FTC, GIPSA does not require investigations to be (1) planned and developed on the basis of how a company's actions may have violated the law and (2) periodically reviewed as they progress by senior officials with anticompetitive practice experience. GIPSA's investigation work is led by regional staff with minimal oversight; headquarters officials generally do not require reviews until investigation cases are developed. We identified nine steps in the process for handling concerns about anticompetitive practices; GIPSA's headquarters performs a review of the case in the sixth step, and OGC is not involved until the eighth step, as shown in figure 1.

Figure 1: GIPSA's Process for Handling Concerns About Anticompetitive Practices



Legend: P&S Act = Packers and Stockyards Act

Note: There are no time criteria for completing any step in this process, except for step six, in which the initial review by GIPSA's headquarters is generally to be completed within 30 days.

*In some instances, the field office sends a case file to GIPSA's headquarters for review for informational purposes. When this happens, the case remains open until the agency's headquarters completes its review.

†Step six is generally the first time that GIPSA's headquarters becomes involved in a case, and step eight is generally the first time that OGC becomes involved.

Source: GAO's analysis based on discussions with GIPSA officials.

According to GIPSA's headquarters and OGC officials, regional staff informally discuss some plans for investigations with them, but the agency does not have specific

requirements for approving an investigation or an investigation plan. These conditions were reflected in the comments of GIPSA's regional office managers and economists, who said that they often have questions about how to interpret the law and how best to scope and perform investigations. Also, OGC officials told us that the anticompetitive practice cases that GIPSA had forwarded often had weaknesses that needed to be addressed before they could determine whether a violation had occurred. Both OGC and GIPSA officials said that OGC's reviews of GIPSA's cases have led to disagreements about interpretation of the act and the sufficiency of evidence.

We also found that GIPSA's investigative guidance manual was last revised in 1996, prior to the agency's reorganization to develop anticompetitive practice investigation capabilities. The manual does not contain specific guidance for anticompetitive practice investigations, such as the contents of an investigative plan, the information needed for approval of an investigation, or the frequency of reviews of the investigations.

In our report, we concluded that GIPSA needs to adopt a more systematic approach to planning and performing investigations. An approach similar to DOJ's and FTC's would start with a preliminary phase to develop a theory of the alleged violation and a plan of investigation. At this stage, senior officials within GIPSA and OGC would approve the initial theory of the case, the plan, and the commitment of resources. Thereafter, periodic reviews would be held at major decision points. If GIPSA and OGC officials consult with DOJ and FTC officials, they may obtain suggestions about how to promote teamwork on investigations and ideas about how to shape a program suited for GIPSA's and OGC's workload and organizational structures. Therefore, we recommended that the Secretary of Agriculture improve GIPSA's investigation processes and practices by adopting methods and guidance similar to DOJ's and FTC's for selecting, planning, conducting, and reviewing investigations. In doing so, we recommended that the Secretary (1) provide for senior GIPSA and OGC officials to review the progress of investigations at main decision points and provide feedback, guidance, and approval of investigations as they progress, and (2) consult with the Attorney General and the Chairman of the Federal Trade Commission on investigation management, operations, and case development processes.

GIPSA's Authority Under the Packers and Stockyards Act

The Packers and Stockyards Act⁵ prohibits packers⁶ from engaging in or using any unfair, unjustly discriminatory, or deceptive practice or device, or making or giving any undue or unreasonable preference or advantage to another party.⁷ The act does not define "unfair practices" and consequently what is unfair must be determined by regulation or on a case-by-case basis by applying "a rule of reason." To prove that a practice is unfair, GIPSA must show that the packer intended to injure another party (predatory intent) or that its action caused injury (e.g., injury to competitors) or is likely to do so.

In addition, the Packers and Stockyards Act specifically makes unlawful packer anticompetitive practices that are antitrust-type actions, including a packer's activities that manipulate or control prices or restrain trade. To prove that such an activity has occurred under the act, GIPSA, in most instances, must show that the purpose of the packer's action or its actual effect was to carry out the prohibited activity. GIPSA may also choose to treat such activity as an unfair practice, which may be easier to prove than a violation of the act's antitrust-type provisions. Also, while mergers are a concern because they can reduce competition, the act does not provide USDA with premerger review authority.

The act allows GIPSA to start investigations and administrative actions to halt packer practices that it deems to be unfair or anticompetitive. When an investigation finds and develops evidence to show that a packer may have engaged in an anticompetitive or unfair practice, GIPSA may file a complaint against the packer. The packer has a right to a hearing, which is held before a USDA administrative law judge. If, after reviewing the evidence presented by GIPSA and the packer, the administrative law judge decides that there has been a violation of the act, a cease and desist order may be issued, and a civil fine may be levied. An administrative law judge's decision can be appealed to USDA's

⁵A more detailed discussion of GIPSA's authority under the act, including references to statutory and regulatory provisions and court decisions is contained in appendix I of our September 21, 2000, report.

⁶The act defines the term "packer" to include any person who in commerce (1) buys livestock for slaughter; (2) manufactures or prepares meat products for sale or shipment; or (3) markets meat, meat products, or livestock products in an unmanufactured form as a wholesale broker, dealer, or distributor.

⁷It is also unlawful under the act for any stockyard owner, market agency, or dealer to engage in any unfair, unjustly discriminatory, or deceptive practice in connection with, among other things, the marketing, buying, or selling of livestock on a commission basis. The Secretary of Agriculture may, pursuant to a complaint or on his own initiative, bring an administrative action to halt such practices.

Judicial Officer, who acts on behalf of the Secretary of Agriculture. The packer, but not USDA, may file a further appeal to a Federal Circuit Court of Appeals.

In our report, we concluded that GIPSA has strengthened its program since 1997 by reorganizing to focus on specific livestock industries. Also, GIPSA's economists, with some experience and guidance, will enable the agency to be more effective in its investigations of complicated market issues. Presently, however, GIPSA is better positioned for performing economic analyses than fully developing the complete cases needed to prove that anticompetitive practices have occurred. We also noted that DOJ, FTC, and GIPSA have been involved in monitoring the industry and have taken producers' concerns into account. We believe, however, that GIPSA and USDA's OGC need to continue improving their investigative capabilities and processes.

GIPSA also has an important role in periodically keeping the industry and the Congress informed about its monitoring of livestock markets. Since GIPSA's last major report in 1996, there have been further dynamic changes in the cattle and hog markets. These changes involve integration within the industry and changes in market operations and production margins. GIPSA could further help shape the understanding and views of industry participants by reporting again on such changes and by providing its perspective on issues involving competition. Therefore, we also recommended in our report that the Administrator, GIPSA, provide industry participants and the Congress with clarifications of GIPSA's views on competitive activities by reporting publicly on changing business practices in the cattle and hog industries and identifying market operations or activities that appear to raise concerns under the Packers and Stockyards Act.

USDA reviewed a draft of our report before it was issued and concurred with our report and recommendations. USDA's written comments discussed actions that GIPSA and OGC are taking or planning to take to improve investigations of anticompetitive practices. Specifically, USDA said, among other things, that it (1) will seek to formalize consultations between GIPSA and OGC on complex investigations of anticompetitive practices, and integrate OGC's attorneys into GIPSA's investigative teams early in the investigative process; (2) will adopt relevant portions of the procedures used by DOJ and

FTC for planning, developing, implementing, and reviewing investigations; and (3) anticipates developing a tiered review process for investigations in which routine investigations are subject to oversight by GIPSA's headquarters and complex investigations are subject to review and approval by GIPSA's headquarters and OGC. In addition, USDA also agreed that GIPSA could report on how the Packers and Stockyards Act applies to market activities and identify those activities that raise concerns about fairness and competition.

Mr. Chairman, we believe that the implementation of our recommendations will improve GIPSA's capabilities, processes, and practices for investigating alleged anticompetitive practices. These improvements will reflect a more vigilant and skillful federal presence and instill greater confidence that industry's concerns will be investigated fairly and diligently.

Mr. Chairman, this concludes our formal statement. If you or other Members of the Subcommittee have any questions, we will be pleased to respond to them.

Contact and Acknowledgment

For future contacts regarding this testimony, please contact Lawrence J. Dyckman on (202) 512-5138. Individuals making key contributions to this testimony and/or to the report on which it was based include Charles M. Adams, Patrick J. Sweeney, Alan R. Kasdan, Gary T. Brown, Larry D. Van Sickle, Fredrick C. Light, and Mary C. Kenney.

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